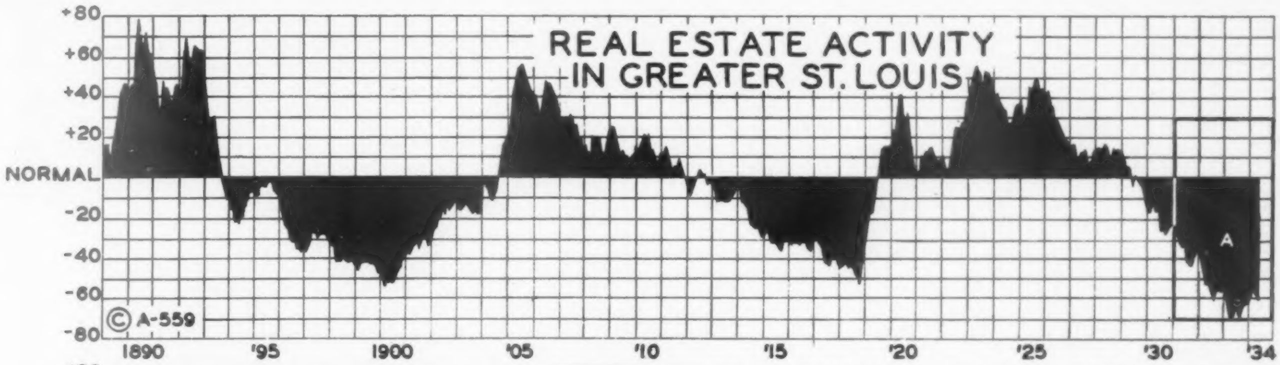
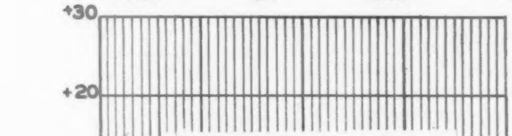
JULY, 1934

The Real Estate ANALYST

SAINT LOUIS EDITION





THE summer recession is proving slightly greater than seasonal. This is true not only of general business but also of real estate. For the first time this year, the vacancy figures for Saint Louis are higher than they were the preceding month. The 13,500 vacant residential units in the city on June 6 had increased to about 14,000 by July 5. We think that a portion of this is seasonal, representing teachers and others who go away for the summer and give up their apartments. Part of it, however, is due to the fact that the demand for increased space has been halted temporarily due to the slowing up of business.

For the first time in nine months foreclosures advanced. We think that this is due to the fact that during the past few months many foreclosures have been delayed with the hope that the HOLC could work them out. With the final rejection of a number of these cases, an increase in foreclosures became inevitable.

General real estate activity, as shown on the chart to the left, fell from 57.7% to 60.5% below normal. Marriages showed a very slight advance. Rentals, new building and building costs showed relatively little change over the preceding month.

What does this recession indicate? We believe that it is to be expected that progress as rapid as has been made during the last year will be interrupted from time to time by recessions of greater or less importance. Turn to page 184 in the September, 1933 issue and notice that the very rapid recovery in 1879 was interrupted by a drop in activity and a rise in the foreclosure rate. In 1901 there were several slight interruptions in the improvement after the depression of the nineties, accompanied by a slight rise in the foreclosure rate.

We hope these recessions will be slight, but with the effects of the drought in the United States and the very disturbing influences in Germany, we should not be greatly surprised if recovery were halted until fall. The purchase of real estate is optional, and any factors which lessen confidence in the future postpone the assumption of the financial obligations generally involved in its purchase.

THE NATIONAL HOUSING ACT AND REAL ESTATE

THREE intended stimulants for new building were launched by the Administration during June. In the order of their importance these were: 1, The National Housing Act signed by the President on June 27; 2, The executive order of the President signed June 30, allowing bidders on government work to submit bids as much as 15% below the filed code price; and 3, The drive on the construction material manufacturers and labor for lower building costs.

How will these "stimulants" affect new building and real estate values?

THE NATIONAL HOUSING ACT

The National Housing Act covers twenty-three pages of fine print. In addition to the features we will discuss here, it carries provisions for National Mortgage Associations, the insurance of saving and loan accounts, and amendments to the Home Loan Bank Act and the Federal Reserve Act. It contains three provisions with which the owners of real estate should be primarily concerned.

I. MODERNIZING AND REPAIR

The first sets up a fund of $200,000,000 to insure against loss, without cost except to the government, acceptable lending institutions making loans of not over $2000 each for repairs, alterations or improvements to real property. The maximum loss allowed to any institution will be 20% of the total amount of the loans made by it. The loan is made on a note and does not require a mortgage. The purpose of this Act is, of course, to stimulate employment of building labor. Its operation is limited to the next year and a half.

With twenty percent of their possible losses guaranteed there can be no question but that lending institutions will be willing to take greater chances than they otherwise would. This will therefore result in some increased employment and the restoring to first class condition of some properties now badly in need of attention. It must be remembered, however, that the competition for tenants during the period of high vacancy caused a great deal of modernization and repair work, leaving rented quarters on the whole in relatively good condition at the present time. Many owner-occupied buildings are not in as good repair as they were before the depression, but these buildings constitute only a little more than a third of urban residences. In the great majority of these cases, the financial distress of the equity holder is the reason for the present state of ill repair. These owners cannot be expected to apply for loans of this sort and if they do their applications will naturally be refused by any rational loan agents.

We understand that this is to be a "high pressure" campaign with state chairmen, local chairmen and committees of local citizens to create popular appeal. Jas. A. Moffett, Housing Administrator, made the statement to the press that the modernizing program would put five million men to work. Many "high pressure" modernization campaigns in the past have apparently succeeded because of two factors: 1 - during the campaign careful totals were kept of all work done and in a short time these totals rose to impressive heights. Critical inspection of many of these cases, however, has convinced us that much of the work for which the campaign got credit was normal maintenance and repair work which would have been done on the same scale, but unreported, had there been no campaign. 2 - A short campaign of this sort naturally moves forward some work, concentrating in three months, for instance, work which would normally be done during a six months period. Whether a campaign over a longer period can sustain interest and move forward enough work by a period of years is subject to grave doubt. We therefore seriously question the effectiveness of these provisions of the Act in stimulating any great amount of <u>additional</u> employment. We believe that it will be possible to compile figures for maintenance and repair work for the next year and a half which will sound quite convincing to one not acquainted with the regular volume of this work.

II. MUTUAL MORTGAGE INSURANCE

The second portion of the Act with which we are concerned is that section providing for the establishment of a "Mutual Mortgage Insurance Fund". This portion of the Act makes it possible to fully insure a lender against financial loss on any mortgage made in accordance with the provisions of the "Fund". The mortgage may be for any amount up to 80% of the appraised value of the property; may run for as long as twenty years; must contain complete amortization provisions; must not, except under certain special conditions, carry more than 5% interest; must be on a building used wholly or in part as a residential building, designed for not more than four families and appraised for not more than $20,000, or a larger building designed to

provide low-cost housing. The building may be old or new. A commitment may be secured for insurance on a construction loan. A construction loan, if it has a maturity of not to exceed six months, may be classed as an ordinary commercial loan subject to discount by a member bank with the Federal Reserve. The insurance rate must not be less than one half percent a year and not more than one percent, depending on the risk. Insurance premiums collected in excess of requirements will be credited eventually toward the amortization of the loan.

We believe that this portion of the Act will revolutionize home financing. It will do away with the greater part of second mortgages with their high discount rates. It will lower interest rates to not more than five percent. It will reduce the percentage of unamortized loans on real property. It will liquify mortgages. It will loosen credit for real estate. It will eventually lessen the cost of shelter for the average American family.

We think that the advocates of this Act are going to be sadly disappointed, however, with its emergency value. We believe that this Act will not be the immediate stimulant to new building which they intended. In the first place, it will take some months to set up the necessary credit insurance machinery. After it is set up, there will be some question regarding the reception it will get from the investing public. The investor, accustomed to buying unamortized mortgages on residential property, will find himself faced with a situation which will cut his percentage of return tremendously. The drop in the interest rate to 5% is not an obstacle to securing money but the repayment of the principal in small payments will make it impossible for the average investor to keep his entire principal employed. If he wishes to keep his principal intact he must accumulate these small amortization payments until they are again of sufficient size to re-invest. This will not affect the larger investor or the Building and Loan Associations, altho we believe that the Building and Loan Associations will be forced to go to a longer amortization period. Unless the small real estate loan broker can adapt himself to these new conditions, he will find his volume greatly reduced by the National Mortgage Associations, the Building and Loan Associations and larger investment companies. On page 288 in this issue is a discussion of the probable cost of financing under this plan.

After this readjustment of the financing methods and agents, which will take time, insured loans will undoubtedly make credit available for building, but in our opinion availability of credit alone will not start any appreciable volume of building. Unless the cost of building can be lowered materially, new building will proceed at very low levels. In order to start any great volume of residential building at the present time, it would be necessary to bring the completed cost of a new building down to a level where it could compete with the homes already on the market, forced to low levels by excessive vacancy, high taxes, high foreclosures and low rentals. If this could be done it would stimulate new building but it would also make impossible the recovery of the older properties with which new buildings would compete. Foreclosures would again rise to record heights and would stay there until existing properties had been completely liquidated to a lower level.

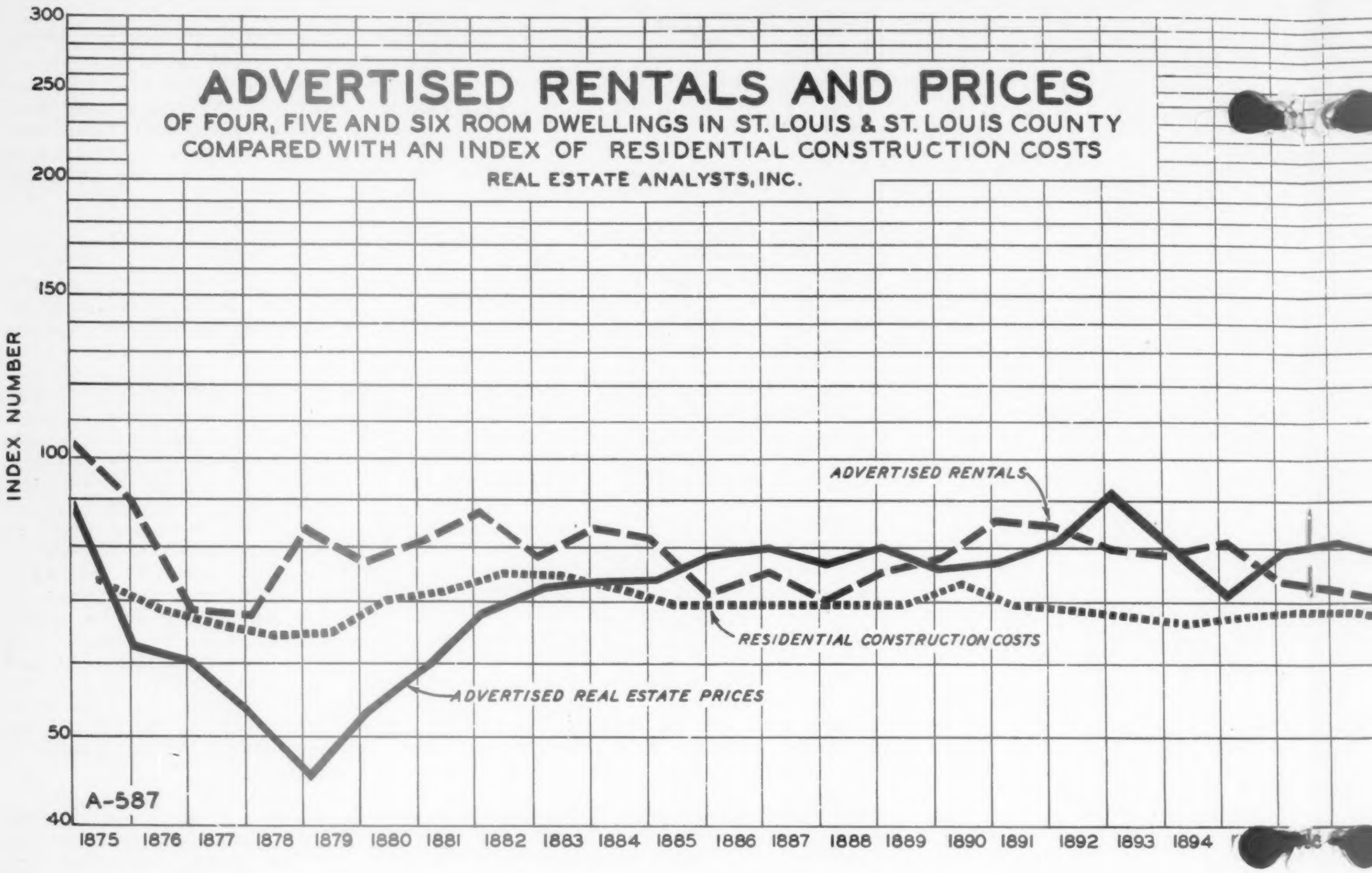
III. REDUCTION IN FREIGHT RATES

The Administration realizes that the high cost of building is the greatest obstacle to employment in the building trades and is trying to reduce this cost. The third provision of the Housing Act in which we are interested in this analysis attempts to reduce the cost of building materials by permitting carriers to give reduced rates to this type of commodity if authorized by the Interstate Commerce Commission. However, other provisions passed by the last Congress have increased materially the operating expenses of the railroads and it seems unlikely to us that it will be possible to greatly reduce freight charges on building materials. But suppose for a few minutes that freight rates could be cut 20%. Calculations we have made would indicate that this would lower the delivered price of steel in Saint Louis by 2%; the price of a 395-pound enameled bath tub with fittings, costing \$56.70, by 80¢ or 1.4%; lumber and millwork by about 2 to 3%; cement by 2%; brick by 3 to 4%. The total cost of the house would be reduced by about 1%. If building materials were transported free by the railroads it could not reduce the finished cost of the house by as much as 5%. After the very rapid increases of the past year, microscopic reductions such as these will not start a building boom.

THE EXECUTIVE ORDER ON GOVERNMENT CONTRACTS

In an effort to reduce building material prices still further, President Roosevelt on June 30 signed an executive order allowing bidders on government contracts to submit bids as much as 15% below the filed code prices. As soon as the bids are opened the prices bid on the government contract become the new prices to the private consumers as well. This order, however, does not abrogate the other pro-

(Continued on Page 288)



THE chart above is an effort we have made to approximate the fluctuations of real estate prices over a long period of years. We are under no mistaken idea that the index we have arrived at shows selling price. We make no claims for it other than that it is the best index we have been able to construct so far giving any idea of how asking prices have varied for four, five and six room single family dwellings over a long period of years.

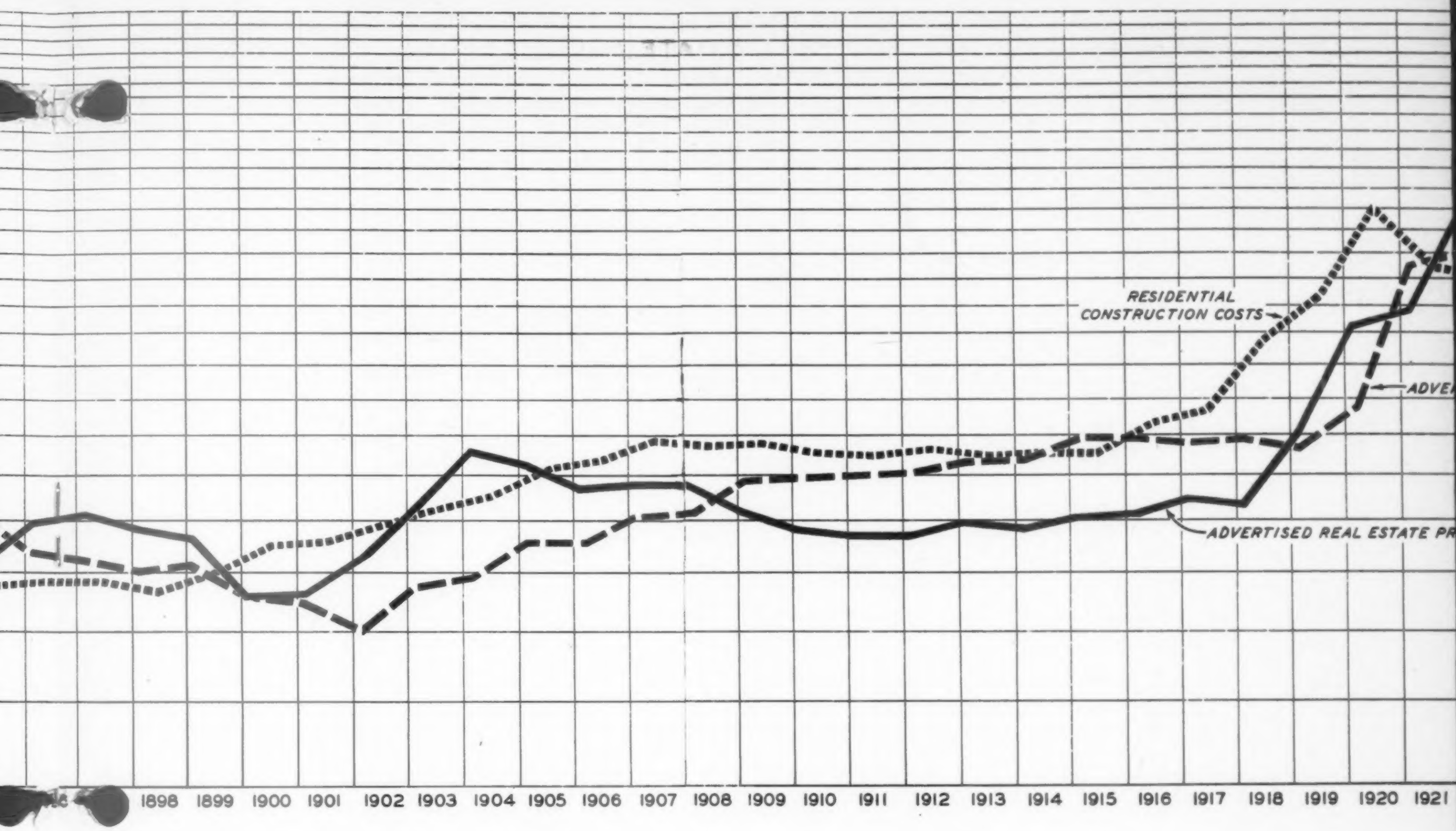
This index was prepared in the following manner: The average advertised selling prices were computed from the classified "for sale" advertisements in the newspapers for four, five and six room single family dwellings. These averages were next combined into a single index which is shown by the solid line on the chart above.

With this index of advertised prices are shown two other lines, one of average advertised rentals of four, five and six room single family dwellings and the other an index of the cost of building a residential building.

It will be noticed that this rental index is quite different from that shown in other issues of the Real Estate Analyst. This is due to the fact that this index does not include the smaller or larger dwellings. As there is practically no vacancy at the present time in four, five or six room dwellings and as the vacancy in this type of building was never excessive, the line did not decline as much as it otherwise would and is now moving rapidly upward. Our regular index has not made as large an increase because of the rather large vacancy still existing in the older large single family buildings.

It will also be noticed that the index showing advertised prices has stopped going down. We believe it is now on the verge of a rapid increase.

The index of building costs has been advancing sharply for the last year. It is rising at the present time at a faster rate than it rose during the World War. Many efforts are being made to halt its rise until new building can get under way,



but we expect it to continue upward at a fairly rapid rate during the next few years.

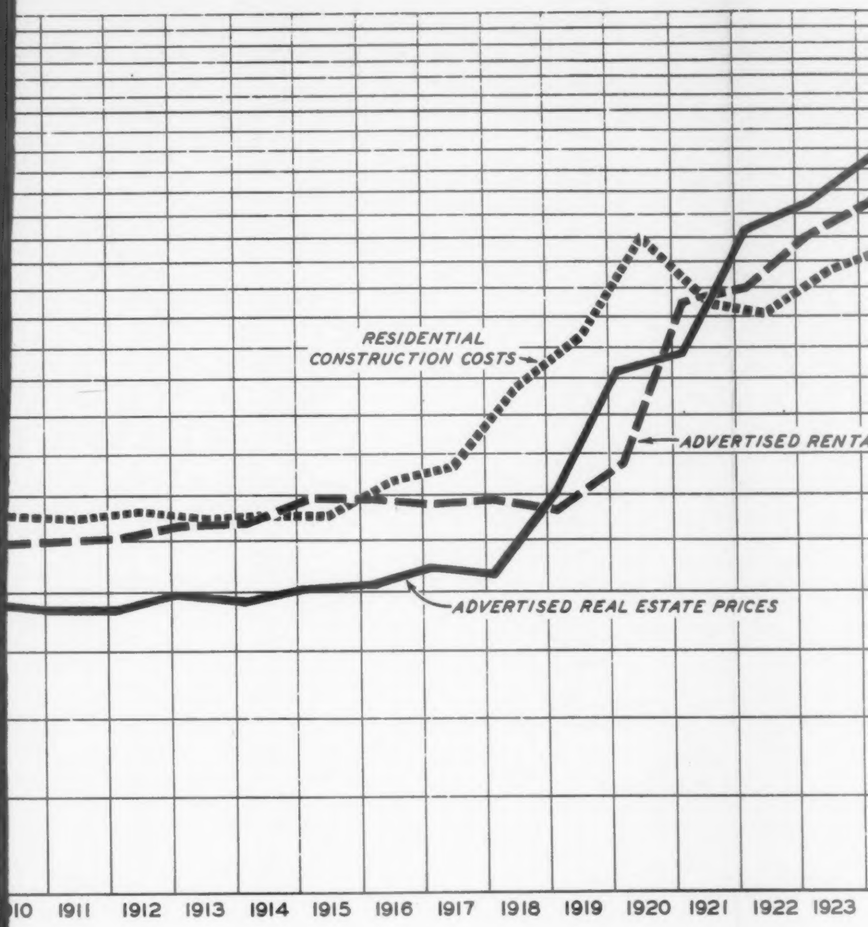
The self-evident limitations of a study of real estate prices based on newspaper advertisements are as follows:

1. Advertised prices, especially during a depression, do not represent the prices for which property is actually sold for cash, as trading on an inflated basis keeps the asking price much above the cash selling price. How great a factor this formed in past depressions is not known at present.

2. Four, five and six room single family dwellings have experienced relatively little vacancy and have, therefore, withstood price adjustments a great deal better than flats and apartments. On the other hand, these are the only classes of dwellings for which a sufficient number of "for sale" advertisements appear over the entire period. It should also be remembered that the small residence has advanced tremendously in social standing during the period covered by this chart. Thirty years ago a four, five or six room residence was a "cottage" in the estimation of the greater part of the population. All buildings of any standing contained from nine rooms up.

3. Insufficient "for sale" advertisements giving price were found prior to 1875. This makes it impossible to chart advertised price figures prior to that year. It is peculiarly unfortunate that this line cannot be carried back ten years further as it would then include the readjustments after the Civil War monetary and credit inflation. The few advertisements which did appear giving prices in these years would indicate that during the early seventies advertised prices on our chart would be above the line indicating advertised rentals. If such were the case it would present a picture very similar to the period from 1925 to 1934.

4. Advertised rentals do not represent actual rentals in a period of depression, due to the almost universal custom of giving a concession in the way of a free period with a lease. In a period of inflation it is believed the advertised



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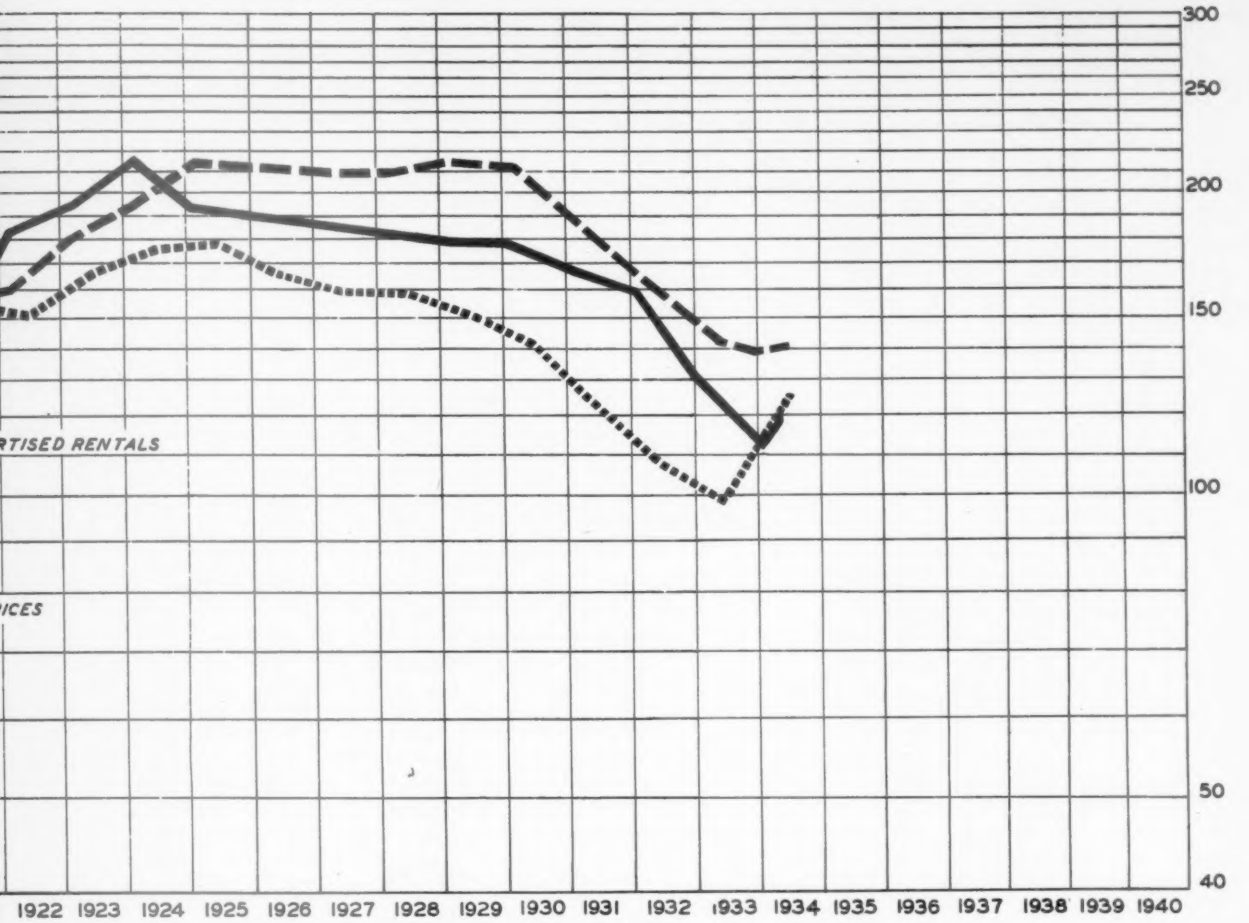
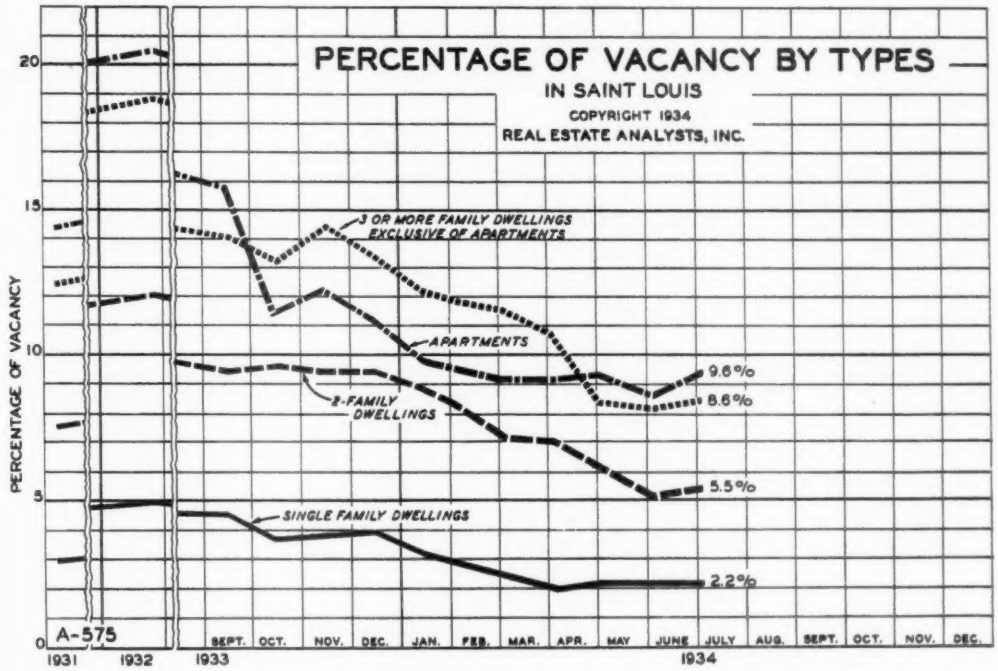


and actual rentals are very close together.

With the foregoing limitations in mind, let us look at the chart again to see what it might suggest.

1. Without exception each increase in advertised prices of real estate has been preceded by an increase in advertised rentals. The great depression after the Civil War started in 1873 and in 1875 rentals started dropping, continuing their drop until 1878, when they again started up. Values dropped for one year longer than rentals, not starting their upward climb until 1879. The depression in the nineties resulted in a gradual drop of prices and rentals which continued until 1901 when rentals started up, followed again a year later by prices. In 1918 rentals started up and a year later in 1919 prices started to rise. It certainly looks as if the same thing is now taking place in the same order. Rentals have already shown a marked increase on this index and prices have stopped going down. On the basis of the past we should expect advertised prices to show an advance of some size by next year. This is also thoroughly in accord with all of the indications from our other studies. We are firmly convinced that higher prices for real estate are now a matter of but a relatively short time.

2. The increase in rentals and values on four,five and six room dwellings in the period just ahead will be great, but we think it will not be as great as the increase in rentals and values of apartments. Our reason for believing this is that due to the continued demand all during the depression for single dwellings of the more modern type, these dwellings did not undergo the same degree of liquidation either in rentals and prices that the larger multiple family buildings experienced. In the meantime the larger buildings will absorb their vacancy. With a limited supply of the larger buildings for some time to come and with an expanding demand, rentals and prices are certain to rise rapidly once they get under way.



In the table below we show the number of vacant units in the city at various times during 1933 and for the first seven months of 1934.

1933		1934	
March	30,300	January	20,248
October	22,460	February	18,650
December	21,350	March	17,550
		April	16,650
		May	14,700
		June	13,500
		July	14,000

The number of dwelling units absorbed during each of the last seven months is shown in the following table:

December, 1933		1102
January, 1934		1598
February		1100
March		900
April		1950
May		1200
June	-500	
TOTAL - 7 MONTHS		7350

This is an average of 1050 per month. The increase in vacancy during the last month reduced the average considerably. We are inclined to believe that at least a portion of the increase in vacancy is seasonal. As monthly vacancy figures have never been computed before last September when Real Estate Analysts, Inc., started its monthly vacancy check, we do not know whether vacancy regularly increases in July. We think it likely that it should. Saint Louis has approximately five thousand teachers, many of whom leave the city during the long school vacation. Experience has shown that a sizable number of these people give up their living quarters here during the summer. A small number of families in other lines of work where it is possible to enjoy long vacations rent their homes furnished for the summer. It may be that the entire increase in vacancy this last month is seasonal.

THE NATIONAL HOUSING ACT AND REAL ESTATE (Continued from Page 283)

visions of these codes against selling below "allowable cost". A great majority of the codes make it an unfair trade practice to sell below certain well defined "out of pocket expense" of manufacturers. The new executive order specifically leaves to any competitor the right of complaint if the bid price is unfair from the "selling below allowable cost " standpoint. As at the present time the cost clause in the greater part of these codes has actually been setting the sales price, we believe that this order will not greatly affect most of the items which go into a house.

THE NRA DRIVE FOR LOWER BUILDING COSTS

Starting several months ago, the NRA has been making strenuous efforts to lower building costs by conferences with manufacturers and labor. Some slight concessions have been secured. The retail price of lumber, for instance, had dropped on July 1 in this territory by 3%. After the skyrocketing of lumber prices during the past year and a half, a drop of 3% is too small to be of great importance. Some few other items have been reduced by small percentages. The fact remains, however, that manufacturers, required under the codes to pay a larger wage for a shorter period in a market which cannot for several years furnish any sizable volume, cannot lower selling prices.

Building labor, under pressure, may make some nominal concessions - in other words, it may agree to work on small residential buildings at slightly less than the prevailing union scale. Inasmuch as in the greater part of the United States work on this type of building is generally not done by union men, a reduction in the scale to a point still above the price actually being paid will have little effect in stimulating new building.

CONCLUSIONS

These three measures of the Administration are all moves in the right direction. The permanent value of some of them will be great. Combined, the emergency value in creating employment will be slight. The hoped-for revival of the building industry is still some distance in the future. If this were not true, real estate could not expect the great appreciation in price which we confidently expect it to experience.

INTEREST, INSURANCE AND PAYOFF REQUIREMENTS UNDER THE NATIONAL HOUSING ACT

THE National Housing Act specifies 5% interest and complete amortization in not more than twenty years. None of the details of the methods of arriving at monthly payments are given in the Act but are left to the Housing Administrator to work out.

It will probably be decided to handle these loans on a level monthly payment, as this arrangement would give the lowest initial cost to the borrower and would therefore be the most likely to stimulate building. In addition to the interest and amortization payment the act provides for a minimum of 1/2% per year for the insurance of the loan and a maximum of 1%, the rate to vary with the risk. One-half percent would be equivalent to 42¢ per month per thousand dollars. While it is hard to guess what the government may allow the broker as a commission and servicing charge, we think 1/2% as a minimum and 1% as a maximum is likely. The monthly payment necessary to pay 5% interest and amortize the principal in any given number of years can be computed. In the table below we show the possible range of monthly payments, including interest, amortization, insurance and commission and servicing charges for ten, fifteen and twenty year loans per thousand dollars of loan:

	10 years	15 years	20 years
Minimum	$11.63	$8.87	$7.53
Maximum	12.48	9.71	8.35

In the figures shown as "minimum" we figured the insurance premium on the loan and the combined commission and servicing charge at 1/2% each. In the maximum figures we included these items at 1% each.

It is rather interesting to compare these figures with those for other types of financing. Building and loan associations have been working on a base of $11.67 a thousand paying out in about ten and a half years. The Home Owners' Loan

Corporation has been charging $7.91 a thousand for fifteen year loans. It is readily apparent that on a ten year basis the new plan is little different from the building and loan plan. On the fifteen year basis the National Housing Act plan is not as attractive as the HOLC.

It is extremely hard to compare these estimates with present costs under a first and second mortgage. In order to get a comparison it is necessary to figure the cost to the owner, assuming an average residential building. If it were necessary to finance the building 80%, in normal times if the building were new the owner could probably secure a 55% first mortgage. This would leave the balance of 25% for a second at a high rate of discount. In Saint Louis the second mortgage maker would require a 20% discount, making it necessary to sign notes for 30% of the value of the property in order to net the 25% needed. This second mortgage would run for three years with a monthly payoff, probably figured to pay it down to half at the end of that time. The renewal charge then would be from 10 to 15%. The interest on both the first and second mortgages would be 6%. The commission on the first would be 1% a year with a renewal charge at the end of three years of 1/2% a year.

During the initial period, the average monthly cost per thousand dollars for interest on the first mortgage, commission on the first, interest, payoff, discount and renewal on the second would amount to $11.10. Toward the end of the first six years this would be down to $9.91 per thousand. At the end of the first six years the second mortgage would be completely amortized. The 55% loan remaining could be financed with little trouble. This will be especially true in the period immediately ahead as rising values will reduce the percentage of loan to the appraised value of the property.

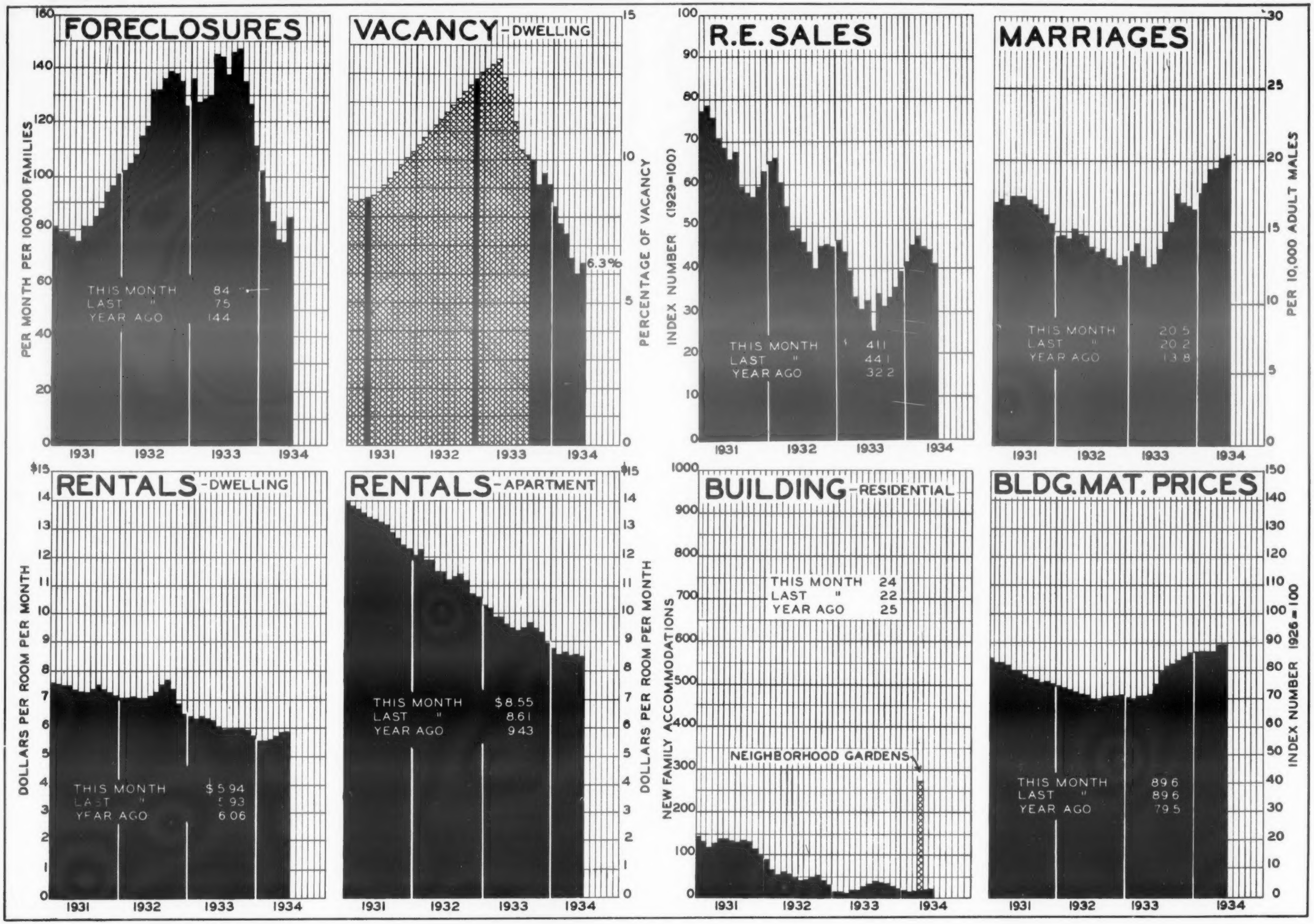
The advantages of the new Housing Act plan are greatest only when loans can be secured for fifteen or twenty years. On a ten year loan the average cost per month will be at least as high as the building and loan rate and higher than the rate necessary with a first and second mortgage. It is true that the first and second mortgage method does not amortize the loan as rapidly but it seems to be human to expect more of the future than of the present, making the monthly cost during the first few years the determining factor in public acceptance.

On a twenty year basis, the same monthly payments will handle an investment approximately 55% larger than can be handled on a ten year basis. Or, putting it another way,on a twenty year basis the same investment can be handled with monthly payments about 35% less than those required on the ten year basis.

If all loans could be made for twenty years, the lower monthly carrying payments would be sufficient to offset the increased cost of construction. If construction costs advanced no further by the time all of the machinery for these new loans was in operation, the building boom would start. However, as explained elsewhere in this issue we do not believe it possible to stop the increase in building material cost and in building labor. It may be halted for a short period, but we are confident that the general trend will be upward for some time to come. We also think that the government may find some difficulty in persuading the private lender, even on an insured basis, to make twenty year loans.

If all loans could be made for fifteen years, the lower monthly payments would make it possible to handle an investment approximately 30% greater than could be handled for the same payments on the ten year plan or the same investment could be carried with payments 24% less than those required on the ten year basis. We do not think that this differential would start a building boom immediately, but it would certainly advance by a period of many months the boom which is sure to come.

Lower interest rates and longer loans will eventually make possible lower rentals in relation to values. During the next few years, however, both rentals and values will rise materially due primarily to decreasing vacancies and to the revaluation of the dollar.


FORECLOSURES
PER MONTH PER 100,000 FAMILIES
THIS MONTH 84
LAST " 75
YEAR AGO 144
VACANCY-DWELLING
PERCENTAGE OF VACANCY
6.3%
R.E. SALES
INDEX NUMBER (1929=100)
THIS MONTH 41.1
LAST " 44.1
YEAR AGO 32.2
MARRIAGES
PER 10,000 ADULT MALES
THIS MONTH 20.5
LAST " 20.2
YEAR AGO 13.8
RENTALS-DWELLING
DOLLARS PER ROOM PER MONTH
THIS MONTH $5.94
LAST " 5.93
YEAR AGO 6.06
RENTALS-APARTMENT
DOLLARS PER ROOM PER MONTH
THIS MONTH $8.55
LAST " 8.61
YEAR AGO 9.43
BUILDING-RESIDENTIAL
NEW FAMILY ACCOMMODATIONS
THIS MONTH 24
LAST " 22
YEAR AGO 25
NEIGHBORHOOD GARDENS
BLDG. MAT. PRICES
INDEX NUMBER 1926=100
THIS MONTH 89.6
LAST " 89.6
YEAR AGO 79.5
1931
1932
1933
1934